

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:B3

PLR-120326-20

Date:

December 03, 2020

### Legend

Distributing =

Business X =

Date 1 =

State Y =

Shareholder A =

Shareholder B =

Shareholder C =

Dear :

This letter responds to your letter dated September 10, 2020. In that letter, you requested that this office reconsider its response to your original letter dated December 21, 2018, as supplemented by subsequent submissions, requesting rulings on certain federal income tax consequences of the Proposed Transaction (as defined below). The information provided in that letter and in subsequent correspondence is summarized below.

This letter is issued pursuant to Rev. Proc. 2017-52, 2017-41 I.R.B. 283, as amplified and modified by Rev. Proc. 2018-53, 2018-43 I.R.B. 667, regarding one or more "Covered Transactions" (as defined in section 2.03(1)(a) of Rev. Proc. 2017-52) under

section 355 and section 368 of the Internal Revenue Code (the “Code”). This Office expresses no opinion as to any issue not specifically addressed by the rulings below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

This office has made no determination regarding whether the Distributions (defined below): (i) satisfy the business purpose requirement of Treas. Reg. § 1.355-2(b); (ii) are used principally as devices for the distribution of the earnings and profits of the distributing corporation or of either of the controlled corporations or of more than one of the three corporations (see section 355(a)(1)(B) and Treas. Reg. § 1.355-2(d)); or (iii) are part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or either of the controlled corporations, or any predecessor or successor of the distributing corporation or either of the controlled corporations, within the meaning of Treas. Reg. § 1.355-8T (see section 355(e)(2)(A)(ii) and Treas. Reg. § 1.355-7).

### **Summary of Facts**

Distributing, a State Y corporation, is engaged in Business X. Distributing made an election under section 1362(a) to be treated under subchapter S with an effective date of Date 1. Distributing has Class A voting stock and Class B nonvoting stock (The Class A and Class B Distributing stock are collectively referred to as the “Distributing Stock”.) The classes of stock differ only with respect to voting rights.

All of the Distributing Stock is owned directly or indirectly by Shareholder A, Shareholder B, and Shareholder C, and their respective children. Each parent, together with their respective children, owns one-third of the Class A stock and one-third of the Class B stock, individually or through revocable and irrevocable trusts. There are various disagreements among the shareholder families as to how the business should be operated and managed.

### **The Proposed Transaction**

For what are represented to be valid business purposes, Distributing proposes to engage in the following transaction (“Proposed Transaction”):

1. Distributing will form Controlled A as a State Y corporation. Controlled A will have Class A voting stock and Class B nonvoting stock. The classes of stock will differ only with respect to voting rights. Distributing will contribute a portion of the assets of Business X to Controlled A in exchange for all of the stock of Controlled

A and the assumption by Controlled A of a portion of Distributing's liabilities ("Contribution A").

2. Distributing will form Controlled B as a State Y corporation. Controlled B will have Class A voting stock and Class B nonvoting stock. The classes of stock will differ only with respect to voting rights. Distributing will contribute a portion of the assets of Business X to Controlled B in exchange for all of the stock of Controlled B and the assumption by Controlled B of a portion of Distributing's liabilities ("Contribution B"). (Contribution A and Contribution B are collectively referred to as the "Contributions".) Immediately after the Contributions, Controlled A and Controlled B will each have a fair market value (assets less assumed liabilities) that is equal to one-third of Distributing's fair market value immediately prior to the Contributions.
3. Shareholder A, Shareholder A's children, and any of their respective trusts ("Group A") will exchange all of their Class A stock in Distributing for all of the Class A stock of Controlled A and all of their Class B stock in Distributing for all of the Class B stock of Controlled A ("Distribution A").
4. Shareholder B, Shareholder B's children and any of their respective trusts ("Group B") will exchange all of their Class A stock in Distributing for all of the Class A stock of Controlled B and all of their Class B stock in Distributing for all of the Class B stock of Controlled B ("Distribution B"). (Distribution A and Distribution B are collectively referred to as the "Distributions".)

### **Representations**

With respect to the each of the Distributions, except as otherwise set forth below, Distributing has made all of the representations in § 3 of the Appendix to Rev. Proc. 2017-52.

(1) Distributing has made the following alternative representations for each of the Distributions:

Representations 3(a), 8(a), 11(b), 15(a), 22(a), 31(a), and 41(b).

(2) Distributing has not made the following representations for each of the Distributions, which do not apply to the Proposed Transaction:

Representations 5, 6, 25, 35, 36, 37, 38, 39, and 40.

(3) Distributing cannot make Representation 23 due to the nature of the business. However, Distributing represents that any mismatch will not result in a material distortion of income and the Distributing shareholders agree to elect to terminate the tax year on the date of the Proposed Transaction pursuant to § 1377(a)(2).

(4) Distributing cannot make Representation 42, but has represented that all of its shareholders are U.S. persons.

Distributing has additionally made the representations set forth in section 3.04 of Rev. Proc. 2018-53 for each of the Distributions.

### **Rulings**

Based solely on the information submitted and the representations set forth above, we rule as follows:

#### Contribution A and Distribution A

1. Contribution A, followed by Distribution A, will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled A will each be “a party to a reorganization” within the meaning of § 368(b).
2. No gain or loss will be recognized by Distributing on Contribution A (§§ 357(a) and 361(a)).
3. No gain or loss will be recognized by Controlled A on Contribution A (§ 1032(a)).
4. Controlled A’s basis in each asset received in Contribution A will be the same as the basis of such asset in the hands of Distributing immediately before Contribution A (§ 362(b)).
5. Controlled A’s holding period for each asset received in Contribution A will include the period during which Distributing held such asset (§ 1223(2)).
6. No gain or loss will be recognized by Distributing on Distribution A (§ 361(c)(1)).
7. No gain or loss will be recognized by (and no amount will otherwise be included in the income of) each member of Group A upon receipt of Controlled A stock in Distribution A (§ 355(a)(1)).
8. The aggregate basis of the Controlled A stock received by each Group A member in Distribution A will equal such Group A member’s aggregate basis in the Distributing Stock surrendered in Distribution A and will be allocated among the shares received in the manner described in Treas. Reg. § 1.358-2 (§ 358(a) and (b)).
9. The holding period of the Controlled A stock received by each member of Group A in Distribution A will include the holding period of the Distributing Stock surrendered in exchange therefor in Distribution A, provided that the Distributing

Stock was held by the shareholder as a capital asset on the date of Distribution A (§ 1223(1)).

10. Earnings and profits of Distributing (if any) will be allocated between Distributing and Controlled A in accordance with § 312(h) and Treas. Reg. § 1.312-10(a).
11. Distributing's accumulated adjustment account immediately before the transaction will be allocated between Distributing and Controlled A in a manner similar to the manner in which Distributing's earnings and profits will be allocated under § 312(h) in accordance with Treas. Reg. § 1.1368-2(d)(3) (§§ 1.312-10(a) and 1.1368-2(d)(3)).
12. The momentary ownership by Distributing of the stock of Controlled A as part of the reorganization under section 368(a)(1)(D) will not cause Controlled A to have an ineligible shareholder for any portion of its first taxable year under section 1361(b)(1)(B) and will not, in itself, render Controlled A ineligible to elect to be an S Corporation for its first taxable year. If Controlled A otherwise meets the requirements of a small business corporation under § 1361, Controlled A will be eligible to make a subchapter S election under § 1362(a) for its first taxable year, provided that such election is made effective immediately following the Proposed Transaction.

#### Contribution B and Distribution B

13. Contribution B, followed by Distribution B, will qualify as a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled B will each be “a party to a reorganization” within the meaning of § 368(b).
14. No gain or loss will be recognized by Distributing on Contribution B (§§ 357(a) and 361(a)).
15. No gain or loss will be recognized by Controlled B on Contribution B (§ 1032(a)).
16. Controlled B's basis in each asset received in Contribution B will be the same as the basis of such asset in the hands of Distributing immediately before Contribution B (§ 362(b)).
17. Controlled B's holding period for each asset received in Contribution B will include the period during which Distributing held such asset (§ 1223(2)).
18. No gain or loss will be recognized by Distributing on Distribution B (§ 361(c)(1)).
19. No gain or loss will be recognized by (and no amount will otherwise be included in the income of) each member of Group B upon receipt of Controlled B stock in Distribution B (§ 355(a)(1)).

20. The aggregate basis of the Controlled B stock received by each Group B member in Distribution B will equal such Group B member's aggregate basis in the Distributing Stock surrendered in Distribution B and will be allocated among the shares received in the manner described in Treas. Reg. § 1.358-2 (§ 358(a) and (b)).
21. The holding period of the Controlled B stock received by each member of Group B in Distribution B will include the holding period of the Distributing Stock surrendered in exchange therefor in Distribution B, provided that the Distributing Stock was held by the shareholder as a capital asset on the date of Distribution B (§ 1223(1)).
22. Earnings and profits of Distributing (if any) will be allocated between Distributing and Controlled B in accordance with § 312(h) and Treas. Reg. § 1.312-10(a).
23. Distributing's accumulated adjustment account immediately before the transaction will be allocated between Distributing and Controlled B in a manner similar to the manner in which Distributing's earnings and profits will be allocated under § 312(h) in accordance with Treas. Reg. § 1.1368-2(d)(3) (§§ 1.312-10(a) and 1.1368-2(d)(3)).
24. The momentary ownership by Distributing of the stock of Controlled B as part of the reorganization under section 368(a)(1)(D) will not cause Controlled B to have an ineligible shareholder for any portion of its first taxable year under section 1361(b)(1)(B) and will not, in itself, render Controlled B ineligible to elect to be an S Corporation for its first taxable year. If Controlled B otherwise meets the requirements of a small business corporation under § 1361, Controlled B will be eligible to make a subchapter S election under § 1362(a) for its first taxable year, provided that such election is made effective immediately following the Proposed Transaction.

### **Caveats**

Except as expressly provided herein, no opinion is expressed or implied concerning the tax treatment of the Proposed Transaction under any provision of the Code and regulations or the tax treatment of any condition existing at the time of, or effects resulting from, the Proposed Transaction that is not specifically addressed by this letter.

### **Procedural Statements**

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter should be attached to the federal income tax return of each taxpayer involved for the taxable year in which the transaction covered by this ruling letter is consummated. Alternatively, taxpayers filing their returns electronically may

satisfy this requirement by attaching a statement to their return that provides the date and control number of this letter ruling.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

Susan E. Massey  
Chief, Branch 3  
Office of Associate Chief Counsel (Corporate)

cc: